Davenport & Company

Town of Leesburg, Virginia

Comprehensive Financial Review

Leesburg
the hometown of the 21st century

February 8, 2016

Background

- The Town of Leesburg (the "Town") entered the credit markets in Spring 2015 to effect both a New Money and Refunding issuance for the General Fund and a Refunding for the Utility Enterprise Fund for a total of $47 million.

- In anticipation of this issuance, the Town met with all three national credit rating agencies: **Moody's**, **Standard & Poor's** and **Fitch**.

  – **Standard & Poor's** affirmed the Town's credit rating to AAA; the highest possible rating.

  – **Fitch** ***upgraded*** the Town from their strong AA+ rating to AAA; the highest possible rating.

  – As part of the Town's 2014 credit review, the Town received a positive outlook from **Moody's** which typically means that if the Town continued on its trajectory, a rating upgrade could be anticipated. Due to the Town's continued positive financial trends and overall trajectory in 2014 and 2015, **Moody's** ***upgraded*** the Town to Aaa; the highest possible rating.

As a result, all three Credit Rating Agencies have the Town of Leesburg as "AAA" – the highest possible rating.

Background

- Interest rates have continued to remain strong. In fact, interest rates are slightly below 9 months ago (i.e. approximate time frame when the most recent Town issuance occurred) despite the Fed increasing the short term federal funds rate.
  - As such, Davenport continuously monitors the Town's Debt Portfolio for possible refunding (i.e. debt service savings) opportunities.

Goals & Objectives

1) Provide an annual update to Town Council on the state of the Town's Finances.

2) The Town of Leesburg as part of its long term sustainability plan/capital improvement plan has identified approximately $7 million of future projects.

   - Davenport has evaluated the effects of the potential borrowing(s) of these capital improvement projects on the Town's Key Debt Ratios/Financial Policy Guidelines.

3) Provide a status report and accompanying strategies for possible debt refinancing(s) for interest rate savings purposes only.

4) Enclosed is a recommended Plan of Finance and timetable designed to meet all of the above goals and objectives. As demonstrated herein, the Plan of Finance continues to meet all of the Town's self-imposed Financial Policy Guidelines, which are critical to maintaining the Town's excellent credit standing.

2015 Bond Sale & Rating Agency Commentary

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- As shown in the table below, the Town's credit rating has improved over the last 20 years in which Davenport has served as Financial Advisor.

	Moody's	S&P	Fitch	
Top Tier "Highest Possible Rating"	Aaa	AAA	AAA	
2nd Tier "Very Strong"	Aa1 Aa2 Aa3	AA+ AA AA-	AA+ AA AA-	(Highest) (Middle) (Lowest)
3rd Tier "Strong"	A1 A2 A3	A+ A A-	A+ A A-	(Highest) (Middle) (Lowest)
4th Tier "Adequate Capacity to Repay"	Baa1 Baa2 Baa3	BBB+ BBB BBB-	BBB+ BBB BBB-	(Highest) (Middle) (Lowest)
5th – 10th Tiers "Below Investment Grade"		BB, B, CCC, CC, C, D		

Current Town Ratings

Initial Town Ratings

Considered Investment Grade

Below Investment Grade

2015 Bond Sale & Rating Agency Commentary

- In April 2015, the Town issued $46.98 million of General Obligation New Money and Refunding Bonds, consisting of three parts.

1) $9.95 million General Fund New Money.

   – The Town borrowed for the New Money Projects over 20 years at an All-In-TIC of 2.73%.

2) $3.82 million General Fund Refunding.

   – The Town saved $290,000 over the life of the loan which equated to 6.49% of the refunded amount on a Net Present Value savings basis, just over double the industry standard 3% Net Present Value Savings minimum threshold.

3) $33.2 million Utility Enterprise Fund Refunding.

   – The Town saved $5.6 million or $250,000 annually over the next two plus decades in the Utility Enterprise Fund or 13.52% on a Net Present Value savings basis.

2015 Bond Sale & Rating Agency Commentary

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- The three national credit rating agencies evaluate all credits based upon 4 primary criteria:

  1) Management;

  2) Finances;

  3) Debt; and,

  4) Demographics.

- The following page(s) includes several comments from the three national credit rating agencies on the above.

- The proposed Plan of Finance maintains all of the various rating agency(s) expectations including the Town's self imposed Financial Policy Guidelines.

2015 Bond Sale & Rating Agency Commentary

- Moody's:
  - "The upgrade to Aaa reflects the Town's solid financial position that has continued to improve and is supported by strong fiscal management and planning."
  - "Our expectation is that the Town's financial performance will continue to remain solid even in spite of a steep increase in debt service in fiscal 2017 due to proactive planning, comprehensive fiscal policies and conservative budgeting practices."
- Fitch:
  - "The rating upgrade to "AAA" from "AA+" reflects the Town's demonstrated ability to achieve strong financial performance and maintain ample reserves. The Town's strong economic indicators further support the "AAA" rating."
  - "An assigned reserve within the general fund was created to prepare for the debt service increase… as part of the budget process, the Town prepared a multiyear financial plan that projects to draw on the debt service reserve fund of $1.0 - $1.5 million annually though fiscal 2020. Given the Town's strong history of conservative budgeting and the modest growth assumptions of the plan, Fitch expects the Town to outperform its projections given anticipated economic, and thus, revenue growth."

2015 Bond Sale & Rating Agency Commentary

- <u>Standard & Poor's:</u>

  – "The Town maintains formal policies in investment and debt management in addition to an adopted reserve policy requiring the Town to establish an undesignated general fund balance at a minimum of 15% of budget."

  – "The Town also maintains a formalized multi-year financial plan. Furthermore, the Town has committed itself to raising its fund balance policy from 15% of expenditures to 20% in the five-year period from 2015-2019; the Town is already above 15%. ***The new formal reserve policy was adopted January 26, 2015***."

  – "In our opinion, the Town's debt and contingent liability profile is very strong with total governmental fund debt service at 7.3% of total governmental fund expenditures."

Fiscal Year 2015 Financial Results

- The Town's Fiscal Year 2015 Audit confirms the discussions the Town had with all three of the national credit rating agencies last Spring.

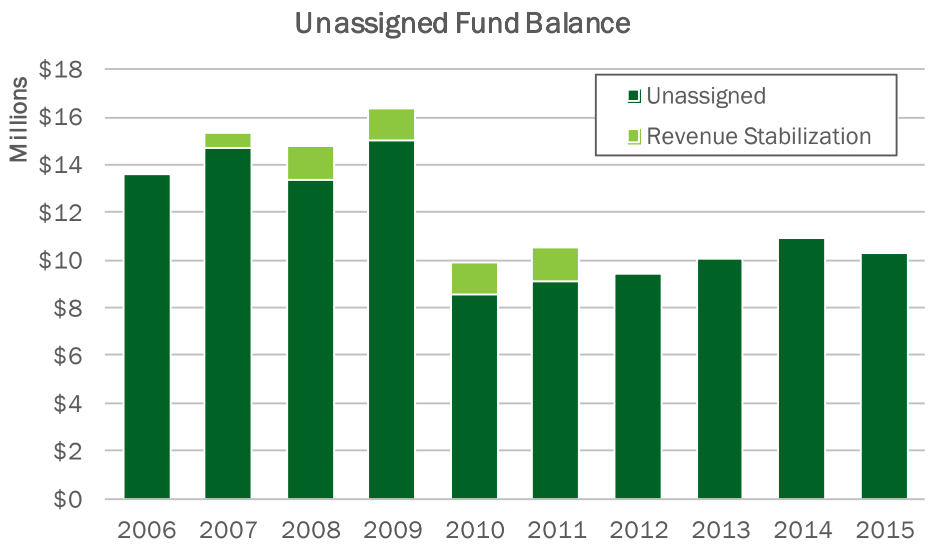
- The Town finished Fiscal Year 2015 with a strong surplus as projected.

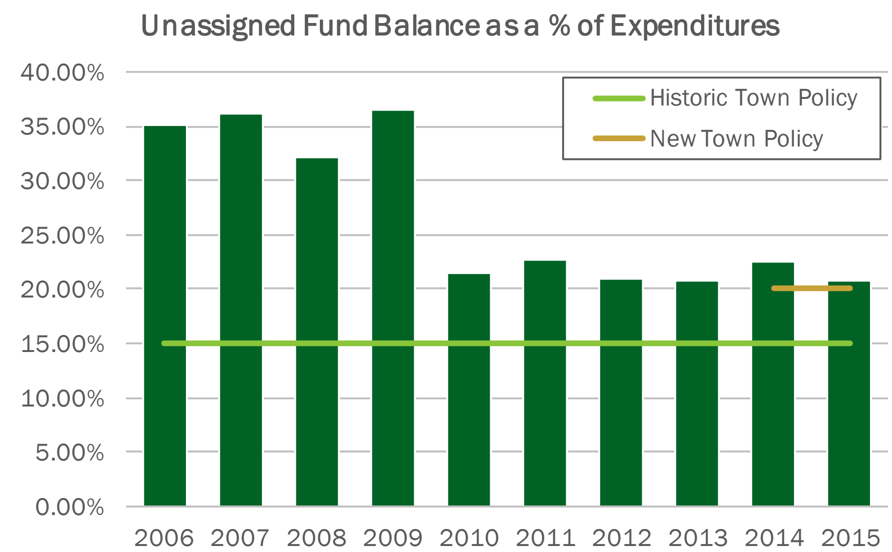
  – Total General Fund Balance increased to $22.8 million from $20.8 million which was greater than the Town's indications for a modest increase to the credit rating agencies.

  – Assigned Debt Service Reserve General Fund Balance increased by approximately $1.8 million from $5.7 million to just shy of $7.6 million.

  – As noted on the subsequent page, the Town's Unassigned General Fund Balance as a percentage of General Fund Expenditures was 20.8%, which is north of the Financial Policy Guideline of 20%.

Unassigned Fund Balance



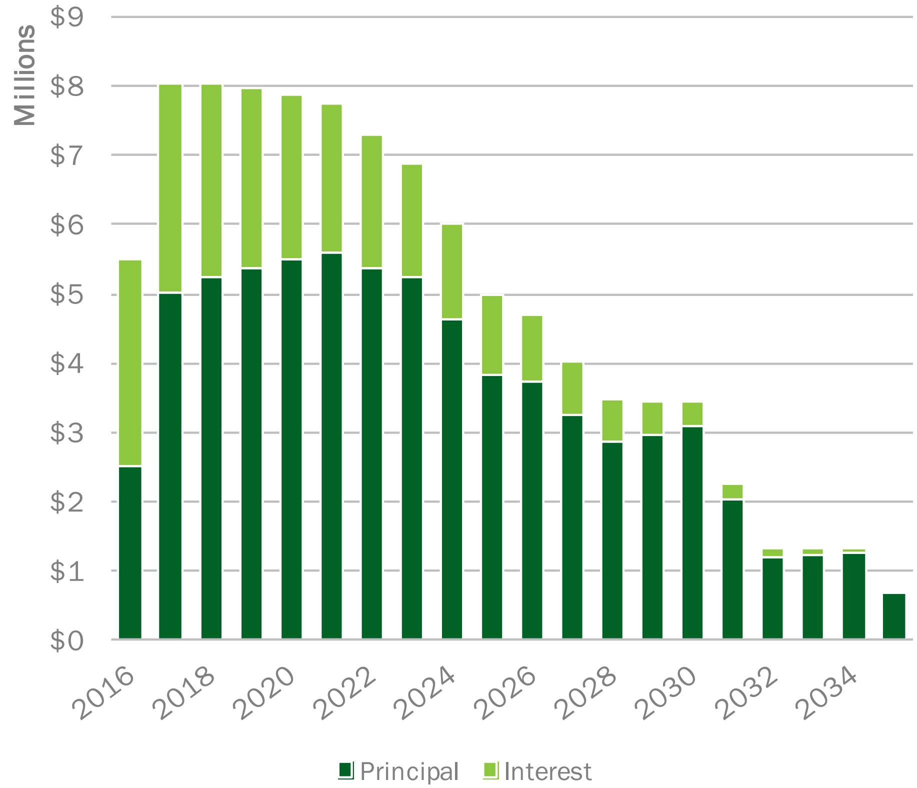


Fiscal Year	General Fund Undesignated/ Unassigned Fund Balance	Revenue Stabilization Fund	Total Fund Balance	General Fund Expenditures	General Fund Unassigned Fund Balance as a % of Expenditures	Town Policy
2006	$13,609,805	$0	$13,609,805	$38,762,859	35.11%	15.00%
2007	14,675,941	700,000	15,375,941	42,456,735	36.22%	15.00%
2008	13,382,816	1,400,000	14,782,816	45,866,109	32.23%	15.00%
2009	14,988,594	1,400,000	16,388,594	44,870,232	36.52%	15.00%
2010	8,529,065	1,400,000	9,929,065	46,142,800	21.52%	15.00%
2011	9,103,329	1,400,000	10,503,329	46,260,493	22.70%	15.00%
2012	9,395,933	0	9,395,933	44,935,479	20.91%	15.00%
2013	10,041,113	0	10,041,113	48,531,008	20.69%	15.00%
2014	10,958,360	0	10,958,360	48,507,451	22.59%	20.00%
2015	10,286,067	0	10,286,067	49,514,193	20.77%	20.00%

Note: The drop in unassigned fund balance from FY 2009 to 2010 resulted from a reallocation of Fund Balance due to changes in GASB accounting standards.

Existing Tax-Supported Debt Service

Tax-Supported General Obligation Debt				
FY	Principal	Interest	Total	Payout Ratio
2016	$2,505,000	$2,997,383	$5,502,383	3.55%
2017	5,020,000	3,009,173	8,029,173	10.66%
2018	5,235,000	2,794,323	8,029,323	18.07%
2019	5,385,000	2,581,984	7,966,984	25.69%
2020	5,505,000	2,365,110	7,870,110	33.49%
2021	5,605,000	2,147,237	7,752,237	41.43%
2022	5,380,000	1,924,953	7,304,953	49.04%
2023	5,235,000	1,654,969	6,889,969	56.46%
2024	4,635,000	1,387,184	6,022,184	63.02%
2025	3,840,000	1,149,221	4,989,221	68.46%
2026	3,740,000	950,760	4,690,760	73.75%
2027	3,250,000	778,451	4,028,451	78.36%
2028	2,860,000	615,955	3,475,955	82.41%
2029	2,965,000	486,513	3,451,513	86.60%
2030	3,075,000	352,237	3,427,237	90.96%
2031	2,040,000	217,450	2,257,450	93.85%
2032	1,180,000	144,669	1,324,669	95.52%
2033	1,215,000	106,231	1,321,231	97.24%
2034	1,260,000	65,938	1,325,938	99.02%
2035	690,000	24,150	714,150	100.00%
Total	$70,620,000	$25,753,889	$96,373,889	



Multi-Year General Fund Debt Issuance(s)

- In early 2015, the Town presented to the three National Credit Rating Agencies the schedule for potential future debt issuances for new money capital needs.

- Following the 2015 issuance, the Town contemplates two additional borrowings:

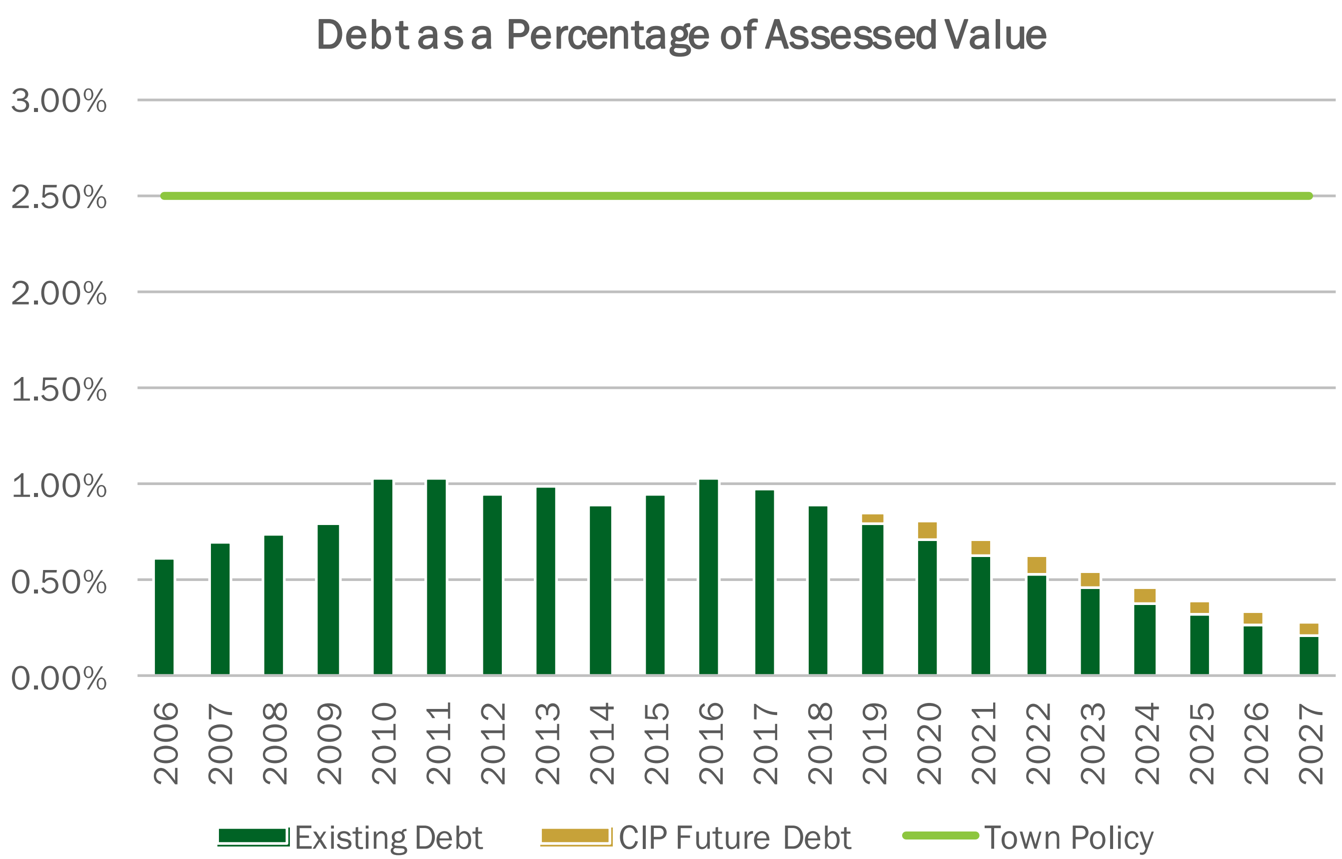
  – Approximately $4 million in Fiscal Year 2019; and,

  – Approximately $3 million in Fiscal Year 2020.

- Both of these potential future issuances have been included in the Town's Key Debt Ratios as outlined on the next page(s).

Debt as a Percentage of Assessed Value

The Town's Debt as a Percentage of Assessed Value is currently well below the Town's Policy of 2.50%



Note: Assumes assessed values grow 2.5% annually beginning in Fiscal Year 2016.
Future CIP Debt includes $4 million issuance in 2019 and $3 million issuance in 2020.
Does not take into account any potential future refunding opportunities.

Debt Service as a Percentage of Expenditures

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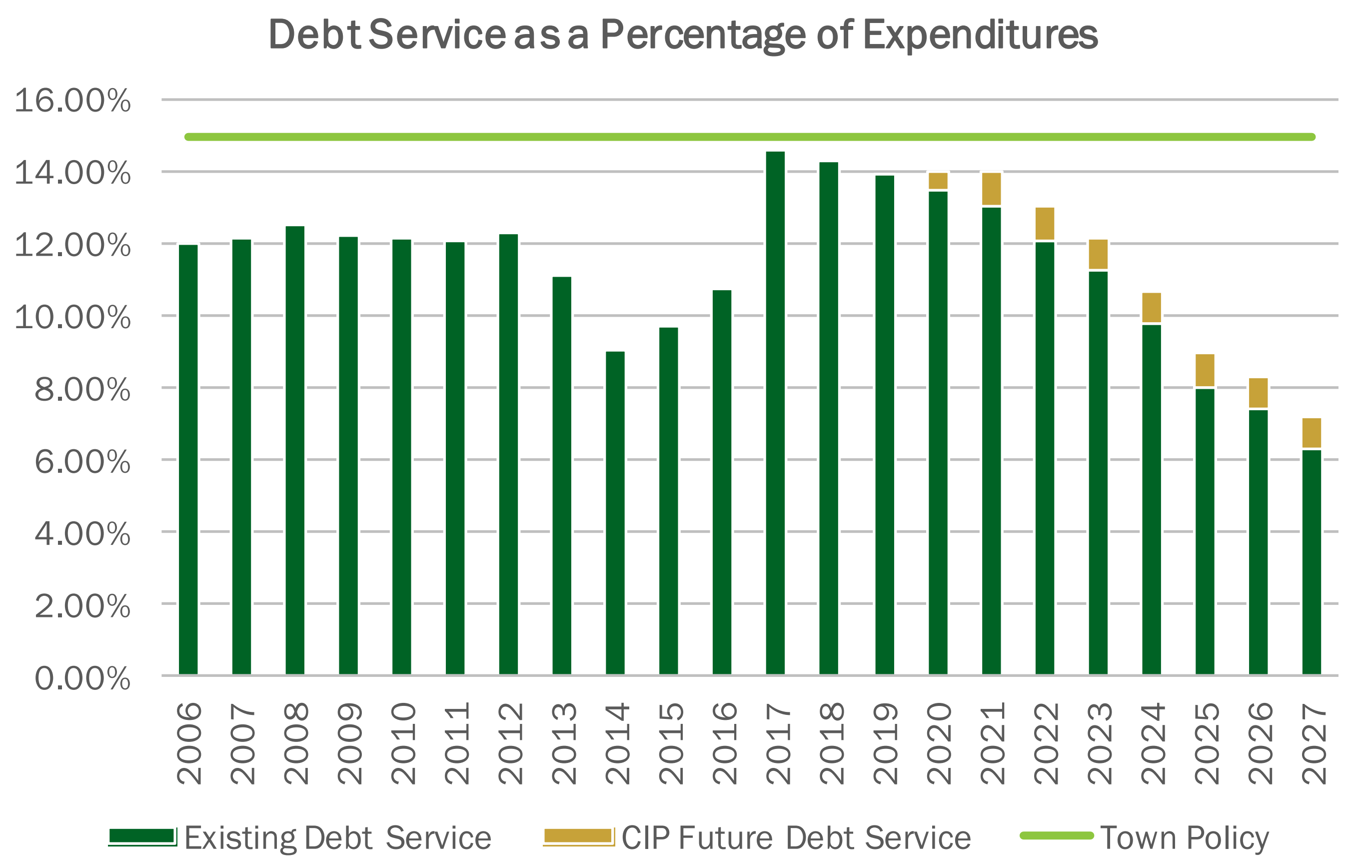
The Town's Debt Service as a Percentage of Expenditures is currently below the Town's Policy of 15%



Note: Assumes General Fund Expenditures grow 2.5% annually beginning in Fiscal Year 2016.
Future CIP Debt includes $4 million issuance in 2019 and $3 million issuance in 2020.
Does not take into account any potential future refunding opportunities.

Debt Affordability versus Debt Capacity

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Debt Capacity versus Debt Affordability:

- **Debt Capacity:**
  - The amount of debt a locality can incur while staying within prudent financial guidelines.
  - Think of Debt Capacity as the credit card limit.
- **Debt Affordability:**
  - The ability of a locality to repay debt obligation with cash flow.
  - Think of Debt Affordability as the ability to pay the credit card's monthly bill.

Debt Capacity

- Of the key debt ratios, Annual Debt Service vs. Expenditures is the limiting factor for the Town.
- Assuming a 20-year level debt service issued at 4.5% and expenditures growth of 2.5% annually beginning in Fiscal Year 2016, the Town could issue tax-supported debt up to the amounts shown below without exceeding prudent financial limits:

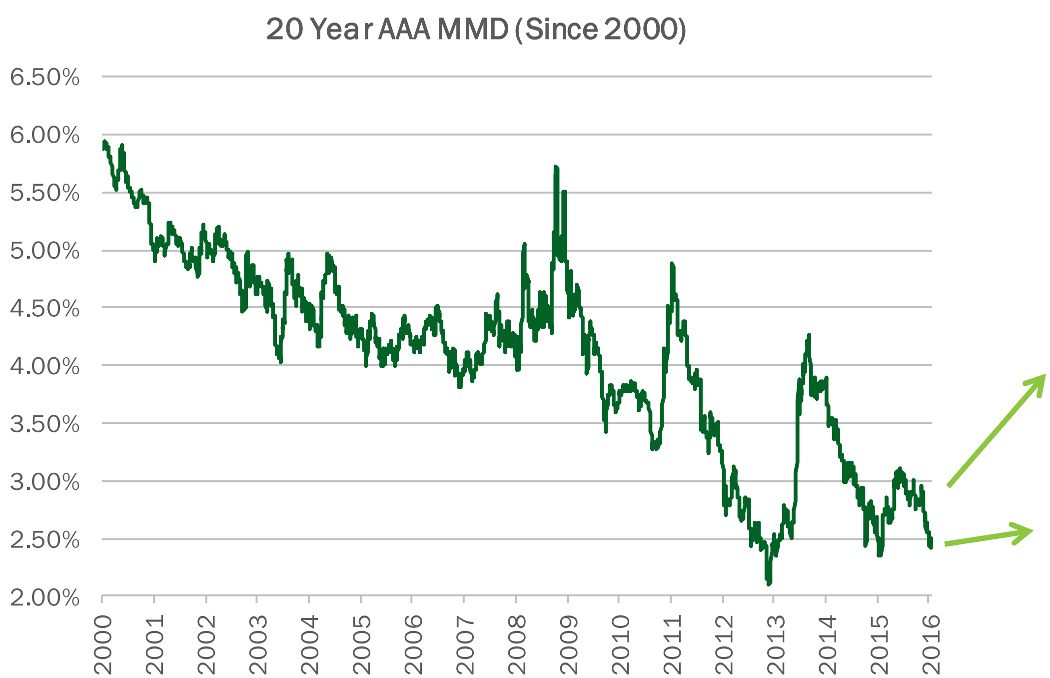
Future Debt Capacity				
First 5 Years				
2017	2018	2019	2020	2021
$2,521,140	$2,226,976	$2,085,117	$0	$473,174
Second 5 Years				
2022	2023	2024	2025	2026
$7,423,524	$7,005,146	$12,173,839	$14,061,052	$5,240,744

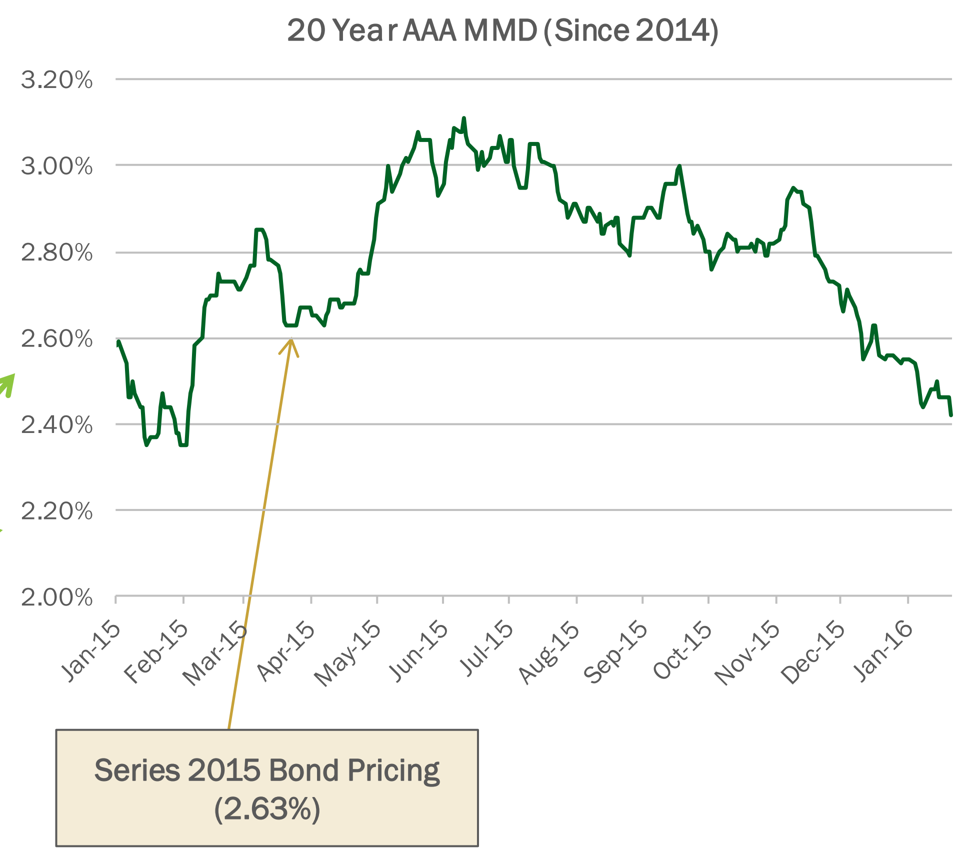
2017 - 2021 Total	2022-2026 Total	10-Year 2017-2026 Total
$7,306,408	$45,904,304	$53,210,712

Current Interest Rate Trends

- Tax-exempt interest rates remain near all-time lows and have been volatile since the beginning of 2015.

- It is unclear how long rates will remain at their current levels.





Note: Rates as of January 25, 2015

Potential Refunding Opportunities

- Davenport monitors the credit markets on a regular basis. As such, Davenport analyzes all of our clients debt portfolio on a continuous basis for debt service (interest rate) savings.

- Typically, a refinancing that produces in excess of 3% on a Net Present Value basis is deemed a reasonable refunding candidate.

- At this time, two potential debt issues have been preliminarily identified as potential refunding candidates. They are:

  – Series 2006B
    – Par to be Refunded: $5,410,000
    – Existing Interest Rates: 5.00%
    – Call Date: September 15, 2017
    – Final Maturity: September 15, 2020

  – Series 2011
    – Par to be Refunded: $11,230,000
    – Existing Interest Rates: 3.75 – 5.00%
    – Call Date: January 15, 2021
    – Final Maturity: January 15, 2041

Estimated Results – Series 2011

- Due to the longevity and final maturity of the loan, the Series 2011 Bonds makes maximum sense as a Virginia Resources Authority ("VRA") issuance via the Spring Pool or a Town Standalone Public Market Issuance – The Dual Track Approach.

- The rationale to refinance the Series 2011 Bonds is that while interest rates are at or near historic lows, the Town could lock in lower fixed rates for the 24 remaining years (i.e. no extension of final maturity).

- The industry standard to gauge whether or not to move forward with a refinancing is 3% net present value savings. The 3% net present value savings threshold would result in $485,000 in net savings which results in approximately $20,000 annually for the life of the loan.

  – Note: The Series 2011 Bonds include proceeds for both the General Fund (67%) and Utility Fund (33%).

- Key characteristics and dates for the Virginia Resources Authority's Spring 2016 Pool and Standalone Public Market Issuance are included on the subsequent page(s).

Series 2011 Dual Track Approach – VRA

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- Apply to the Virginia Resources Authority's ("VRA") Pooled Financing Program Spring 2016 Pool.
- Certain key characteristics of a VRA financing can be summarized as follows:
  - The Town's loan would be financed as part of a larger pooled financing including other state-wide borrowers;
  - **Applying to the VRA Pool in no way obligates the Town to move forward, nor does it cost anything to apply;**
  - The final maturity of the loan could be as long as 30 years and interest rates are fixed for the entire term of the loan;
  - The Town would not be able to prepay or "redeem" the bonds for 10 years, a typical feature of publicly-issued debt.
- Key dates for the VRA Spring Pool are as follows:
  - Applications due by February 5, 2016.
  - Potential sale date projected to be in Early/Mid May 2016.
  - Potential closing date projected to be in Late May 2016.

Series 2011 Dual Track Approach – Standalone

- The key characteristics of a standalone public market issuance can be summarized as follows:
  - Davenport, in consultation with Town Staff, would coordinate with the three National Credit Rating Agencies and prepare a Credit Rating Package.
    - Note: The National Credit Rating Agencies' surveillance of all local governments throughout the United States are moving towards an annual review. As such, in the event the Town elects to proceed with a standalone public market issuance, the Town could satisfy two objectives – meeting surveillance requirements as well as receiving updated ratings for the refunding bonds.
  - Bond Counsel prepares necessary legal documentation including Preliminary Official Statement.
  - Underwriter(s) selected via a competitive process.
    - Davenport to distribute a Request for Proposal to potential underwriters soliciting proposals that would optimize the refunding structure and maximize debt service savings.
  - The Town's maximum out of pocket costs would be in the $30,000 to $40,000 range in the event no refunding occurred in the next 12 – 24 months.
  - A potential advantage is that the Town would be able to effect a refinancing in the next 60-75 days.

Estimated Results – Series 2006B

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- As previously mentioned, the Town's Series 2006B Bonds present a potential refunding opportunity for debt service (interest rate) savings (i.e. no extension of final maturity).

- The industry standard to gauge whether or not to move forward with a refinancing is 3% net present value savings. The 3% net present value savings threshold would result in $172,500 in net savings which results in approximately $43,500 annually for the life of the loan.

- In order to achieve 3% net present value savings, the Town would need to receive an interest rate of 2.39% in order to achieve the desired level.

  – Note: The remaining Series 2006B Bonds were for General Fund purposes only.

- The key features of the recommended approach is summarized on the following page.

Recommended Approach – Series 2006B

- Davenport recommends the Town follow a **"Direct Bank Loan Approach"** in pursuing the potential refunding of the Series 2006B Bonds.

- The Direct Bank Loan Approach means that Davenport, working on the Town's behalf, would:

  1) First, solicit financing proposals from local, regional, and national lenders for the Refinancing Opportunity via a competitive Request for Proposals process.

  2) Then, if necessary, based upon the results, consider waiting until closer to the call period or moving forward sooner.

- Davenport would work as the Town's Financial Advisor to pursue the most favorable possible result, and, as such, would be unbiased as to which direction (moving forward or waiting) would eventually be chosen.

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Appendix

Town of Leesburg, Virginia

Direct Bank Loan Process

- The key characteristics of a Direct Bank Loan financing can be summarized as follows:
  - Davenport, on the Town's behalf, distributes a Request for Proposals (RFP) to solicit competitive interest rate proposals from local, regional, and national lenders;
    - Note: Sending out the RFP in no way obligates the Town to move forward, nor does it cost anything to send out the RFP.
  - **The Town has full control as to when and if to mail a RFP solicitation.**
  - The RFP can specify several different loan term and/or structure options for bidders to provide in their proposals;
  - **The Town has the benefit of knowing the terms and conditions before deciding whether or not to move forward;**
  - Direct Bank Loans often allow for the ability to prepay loan at any time in whole or in part, and sometimes without penalty.

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